

speeches
FDIC
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TESTIMONY OF

L. WILLIAM SEIDMAN
CHAIRMAN
FEDERAL DEPOSIT INSURANCE CORPORATION

ON

THE PROSECUTION OF FINANCIAL CRIMES

BEFORE THE

COMMITTEE ON BANKING, HOUSING, AND
URBAN AFFAIRS
UNITED STATES SENATE

10:00 A.M.
THURSDAY, AUGUST 2, 1990
ROOM 538, DIRKSEN SENATE OFFICE BUILDING

Good morning, Mr. Chairman and members of the Committee. It is a pleasure to be here today to discuss the actions the Federal Deposit Insurance Corporation and the Resolution Trust Corporation are taking to identify and punish those involved in fraud and abuse in the banking and savings and loan industries and to comment on pending legislation to improve prosecutions of financial institutions crime.

The FDIC and the RTC have long put the fight to curtail fraudulent activity in financial institutions at the top of their regulatory agendas. In the last five years, we have developed specially trained fraud squads to pursue those committing fraud and have given our examiners special tools to help in detecting such abuses. Greedy and unscrupulous individuals, insiders, advisors or related parties must not be allowed to profit at the expense of the deposit insurance funds and the American taxpayer.

Our testimony will outline the FDIC and RTC programs to prevent, detect and punish fraud and abuse by individuals and financial institutions. We also will comment on the amendments to the Senate's omnibus crime bill, S. 1970, that address financial institutions fraud and which were adopted by the full Senate on July 11, 1990. Those amendments are designed to provide the banking regulators and law enforcement agencies with additional tools to control fraudulent activities by banks and thrifts and their insiders.

The FDIC and the RTC have authority to bring civil -- but not criminal -- actions against banks and thrifts for fraudulent or other unlawful activities. Our prosecution of civil fraud cases provides an additional significant role in the prosecution of financial crimes. We investigate every failed bank and thrift to determine whether civil or criminal activity was involved in a bank or thrift failure. In addition, our examiners look carefully for evidence of fraudulent activity during the regular examination process of all open institutions. In the case of both failed and open institutions, we refer suspected criminal activity to the appropriate law enforcement agencies.

We also provide much of the basic information needed by the law enforcement agencies throughout all stages of a criminal prosecution. To that end, we participate in the regional inter-agency bank fraud working groups to encourage communication and improve coordination of criminal investigations.

The FDIC also uses administrative enforcement actions to stop fraud and abuse in operating institutions. In addition, the FDIC and the RTC bring civil suits for money damages and restitution (against officers, directors and other insiders) after an institution has failed.

Detecting and Reporting Fraud and Abuse in Open Institutions

FDIC examiners are trained to detect the signs of fraud and other illicit or improper insider actions. Potential problems

often can be uncovered when certain warning signs are evident. In 1987, we developed a list of time tested "red flags" to assist our examiners in the early detection of apparent fraud and insider abuse. The "red flag" list has been expanded once and now is in the process of being updated and expanded again. Examples of the areas that the "red flags" cover include: linked financing/brokered transactions; loan participations; offshore transactions; lending to buy tax shelter investments; and wire transfers. When "red flag" warnings are detected, specially trained members of our "fraud squad" may be called in to pursue the matter using their special training.

Training and role of examiners. New examination personnel begin their careers as Assistant Examiners and usually serve a minimum of three years before they can qualify as commissioned examiners. During these first three years, Assistant Examiners are required to attend four schools that include training in investigatory techniques and detection of insider abuse and fraud. Assistant Examiners also receive on-the-job training in the detection of insider abuse and fraud.

Through the training process, our examiners gain a familiarity with the principal criminal statutes applicable to insured institutions. They also learn how to complete the standard criminal referral forms (Reports of Apparent Crime) used by all financial institution regulators. Additionally, examiners receive instruction on potential problems and warning signs pertaining to bank fraud and insider abuse -- namely, the red

flags. The Division of Supervision's Manual of Examination Policies also sets out alternative investigative procedures appropriate to particular circumstances and addresses the handling of criminal violations when they are discovered.

An examiner's detection of management fraud or other abuse in an operating state nonmember bank generally results in one or more administrative enforcement actions by the FDIC and, in some cases, criminal referrals to the respective U.S. Attorney and the appropriate criminal investigatory agency. Criminal referrals prepared by examiners are reviewed by regional office staff and forwarded to the FBI and U.S. Attorney as soon as possible. However, when examiners detect significant apparent violations, we immediately contact the FBI and the U.S. Attorney by telephone before the examiner prepares the written referral. When requested by law enforcement agents, our examiners will assist in developing evidence and appear as expert witnesses.

Role of institutions. Bank directors and management also bear great responsibility for preventing and detecting fraud and insider abuse. Bank directors must assure that appropriate internal controls are in place. Bank management and employees who suspect a criminal violation are required -- under Part 353 of the FDIC's Rules and Regulations -- to submit Reports of Apparent Crime to the appropriate FDIC Regional Office, the U.S. Attorney, the appropriate State Banking Authority and the appropriate Federal investigative authorities (either the FBI, the Secret Service, the Postal Service, or the IRS) within

thirty days of discovering the suspicious activity. Two different forms are used for this purpose. The Report of Apparent Crime (Short Form) is used to report suspected criminal violations involving less than \$10,000 and suspicious transactions that indicate possible money laundering. The Report of Apparent Crime (Long Form) is used to report suspected criminal violations involving amounts of \$10,000 or greater and all cases, regardless of amount, involving an executive officer, director or principal shareholder of the institution.

Copies of Reports of Apparent Crime involving amounts of \$10,000 or greater, those involving executive officers, directors and major shareholders, and those involving suspected money laundering are forwarded by the regional offices to the FDIC's Special Activities Section in Washington. Those reports are reviewed and certain data from the reports are entered into an automated records system. During 1988 and 1989, the Special Activities Section received 902 and 938 reports, respectively.

The Special Activities Section forwards Reports of Apparent Crime indicating losses of \$200,000 or more to the Department of Justice for special tracking. The individual U.S. Attorneys then make decisions about which criminal cases to pursue. Reports forwarded for tracking totaled 200 in 1988 and 284 in 1989. The Department of Justice enters information from these reports into a computer tracking system and periodically advises the FDIC of their status.

Reports of Apparent Crime filed by banks usually result from such events as teller shortages, false entries, theft, false statements on loan applications, embezzlement or misapplication of funds, check kiting, mysterious disappearance of bank funds, or money laundering.

FDIC "Fraud Squad" Investigations of Fraud

The FDIC has its own "fraud squad." Created in 1986, it is a national investigations unit that investigates fraud and other criminal activities when necessary in operating institutions and in all closed insured banks and in those thrifts that were closed before January 1, 1989. (The RTC's investigatory activities will be addressed below.)

The FDIC's investigations unit is comprised of over 500 investigators and staff. (This number does not encompass attorneys, examiners and other staff who deal with fraud in their day-to-day activities, but who are not full time investigators or support staff for the "fraud squad.")

Investigators receive specialized training in all phases of financial institution operations, accounting, investigative techniques and specific fraudulent schemes. The result is a team of individuals who are well equipped to look into the affairs of failed institutions, as well as operating institutions when called upon to do so.

Each time a financial institution is declared insolvent, an investigative team is dispatched to determine 1) what caused the failure, 2) whether any criminal activity took place and 3) whether any professional liability claims exist. The investigations unit currently is pursuing approximately 942 active claims and investigations.

When possible criminal activity is discovered, the investigators file criminal referrals with the appropriate law enforcement agency. Since 1987, approximately 331 such referrals have been made. The investigators also follow up on these referrals through participation in the local bank fraud working groups. These groups bring together law enforcement personnel and representatives of the financial institution regulatory agencies on a monthly basis to discuss various issues related to bank fraud and other criminal activity. Each of the FDIC's regional offices and consolidated office sites has a designated participant in the local working groups or a contact person for the U.S. Attorney's offices and relevant investigative agencies.

Participation in these groups aids financial institution civil and criminal fraud prosecution in many ways. Few people are as familiar with the records of the financial institution or have the analytical expertise as the investigative team assigned to the failed institution. This expertise is made available in formal and informal ways to aid civil and criminal authorities in discovering, documenting and prosecuting fraud. In some instances, individual investigators are assigned full-time to a grand jury investigation.

The investigations unit also documents and requests restitution pursuant to the Victim and Witness Protection Act when individuals are convicted of crimes involving failed financial institutions.

RTC Investigations of Fraud in Closed Institutions

Investigations unit. The RTC also has its "fraud squad" with a corps of trained, experienced financial investigators. The RTC's Office of Investigations -- which now has approximately 300 investigators and staff -- projects to have 300 investigators alone by year-end. The Office provides the investigatory support to initiate civil and criminal recoveries from thrift owners, managers and professionals -- such as accountants and lawyers -- who caused losses through fraudulent or criminal conduct or professional malpractice. Recoveries can come from insurance policies covering professional conduct or directly from the assets of insiders and professionals. Successful recovery, however, requires thorough investigation and, in many instances, litigation.

The investigator's task is to: gather facts about insider abuse; identify the individuals who caused the thrift's losses; assess the degree of culpability of each party -- from negligent and reckless mismanagement to fraud or criminal conduct -- and help determine whether and what sort of litigation should be initiated to maximize recoveries. Investigators are involved throughout the civil litigation process, supporting the RTC attorneys and outside counsel.

A second, but equally important, responsibility of the Office of Investigations is to assist the Department of Justice and other Federal agencies in prosecuting individuals who engaged in criminal conduct, particularly those who benefited personally at the taxpayers' expense. RTC investigators are being trained to work with law enforcement agents to achieve our mutual objectives. Similarly, law enforcement agents are being trained to understand and respect the RTC's responsibility to recover assets for the thrift receiverships.

The investigator's initial task after RTC is appointed conservator of an insolvent thrift is to conduct a preliminary investigation of the facts leading to insolvency and to prepare a "Preliminary Findings Report." As of June 30, 1990, 397 Preliminary Findings Reports had been completed, representing about 87 percent of the 454 thrifts under the RTC's control.

Insider abuse and misconduct in insolvent thrifts. As a result of our experience over the past few months, we estimate that:

- Approximately 50 percent plus of RTC-controlled thrifts have had suspected criminal misconduct referred to the Department of Justice;
- In about 40 percent of RTC-controlled thrifts, insider abuse and misconduct contributed significantly to the thrift's insolvency;

- About 15 percent of the thrifts appear to have been involved in irregular and possibly fraudulent transactions with other financial institutions.

The average asset size of RTC-controlled thrifts is about \$500 million, and they are complex organizations with numerous subsidiaries and affiliates. Many were owned or dominated by one individual and operated more like real estate development organizations, investment banks, or mutual funds than thrift institutions.

This situation allows for abuse and lack of control. It creates opportunities for self-dealing, fraud, theft and other misconduct to occur unabated. The RTC works with other Federal agencies and, where necessary, retains investigators with specialty skills in securities, commodities, and other disciplines to assist in documenting complex and sophisticated schemes of abuse and misconduct by insiders and other affiliated parties.

Trends and patterns of fraud and misconduct. Evidence of insider abuse and misconduct in RTC thrifts ranges from embezzlement and loan fraud to complex schemes to generate paper accounting profits that allowed cash to flow to thrift owners through subsidiaries or personal holding companies. Many of the complex lending schemes involve over-valued property that was swapped several times between borrowers or among various thrifts. These "land flip" schemes created false values and

generated excessive fees that were parceled out to appraisers, brokers, developers and others -- including thrift insiders. Real estate development loans were made with no recourse to the borrower if the project failed. We are investigating these situations, as well as instances of unauthorized trading in mortgage-backed securities, junk bonds and other financial instruments in which insiders took the profits and pushed the losses onto the institution.

The example of Drexel Burnham Lambert and Michael Milken is a case in point. As announced in June of this year, a special FDIC and RTC task force is actively and aggressively investigating possible claims against Drexel and Michael Milken for substantial losses suffered by failed financial institutions in junk bond investments. Based on preliminary information available to us, we anticipate filing claims in the Drexel bankruptcy proceedings against the \$750 million pool being administered by the Securities and Exchange Commission, and for any civil recoveries available.

Abuses are more prevalent in the Southwest and Southern California. More recent problems are arising in the Northeast and Florida. The RTC's Central Region, comprising Arkansas and 11 midwestern states, reports far and away the lowest percentage of thrifts exhibiting fraud and abuse -- less than 30 percent.

Civil Actions Against Directors, Officers, and
Institution-Affiliated Parties

When an insured depository institution fails, the FDIC or the RTC becomes the legal owner of the institution's claims against its former directors, officers, employees, attorneys, accountants, and other professionals employed by the institution. In the case of every failed institution and those placed in conservatorship, the FDIC or the RTC conducts an investigation of potential professional liability claims. These investigations focus on whether the potential claim is meritorious and, if so, whether it would be cost effective to bring a civil suit seeking money damages.

The Professional Liability Section of the FDIC's Legal Division is responsible for litigating the FDIC's cases involving: directors' and officers' liability ("D&O"); attorney malpractice; accountants' liability; commodity and securities brokers' liability; claims under bankers blanket bonds; and certain appraiser malpractice cases. This section also works in conjunction with the RTC's Office of Investigations to pursue similar actions on behalf of the RTC.

Prior to February 1989, when the savings and loan conservatorship program began, the FDIC had pending investigations of professional liability claims involving approximately 500 institutions. The FDIC also had more than 100 lawsuits on file.

Following the merger with the Federal Savings and Loan Insurance Corporation (FSLIC) in August 1989 and the creation of the RTC -- which formally took over those savings institutions placed in conservatorship after January 1, 1989 -- the FDIC became responsible for the investigation of potential claims and the prosecution of viable claims involving a vastly increased caseload of institutions. The FDIC and RTC currently are conducting investigations in 1300 institutions and have filed more than 500 lawsuits against former directors, officers and other professionals for damages ranging from \$1 million to \$1 billion. The 1300 institutions we have responsibility for in-house can be broken down as follows:

Banks	550 Institutions
Thrifts (old FSLIC)	350 Institutions
Thrifts (RTC)	400 Institutions

In 1989, the FDIC's and the RTC's recoveries for professional liability claims totaled approximately \$100 million. This figure includes old FSLIC recoveries taken in after the August 9, 1989 merger. During 1989, an additional \$50 million in recoveries was received by FSLIC prior to August 9 for professional liability claims. A rough breakdown of these recoveries follows:

FSLIC Thrifts (prior to August 9)	\$50 million
FSLIC Thrifts (after August 9)	\$35 million
FDIC Banks (1989)	\$60 million
RTC Thrifts (1989)	\$4 million

Our recoveries for the first quarter of 1990 alone total more than \$100 million. When I testified three weeks ago before the House Judiciary Committee, I noted that settlements and judgments during the first half of 1990 will produce recoveries totalling in excess of \$200 million, or more than \$1 million per day. I am pleased to report that, as of July 31, 1990, our 1990 recovery figure is approaching \$300 million.

Over the past few years, the FDIC has litigated claims involving approximately 50 percent of those institutions for which it has been appointed receiver. This percentage of claims in litigation may drop somewhat -- particularly as to the RTC thrifts -- because of a scarcity of recovery sources, including D&O insurance and personal assets among many of the potential defendants.

The FDIC and the RTC contract with approximately 150 law firms to prosecute professional liability claims. Our in-house attorneys supervise and manage this litigation to ensure consistency in arguing legal issues and conformity to case plans and budgets, among other things. In-house attorneys also directly conduct settlement negotiations involving claims.

Much of the litigation now pending in the Professional Liability Section involves claims brought against former directors and officers who managed the failed institutions. These claims range from fraud and insider abuse to grossly negligent failures to conduct or supervise the financial institution's affairs.

Although historically many of the FDIC's cases are based on abusive lending practices, that is not the only basis for filing suits. We also have brought suits based on the payment of unreasonable dividends, imprudent or illegal investments in bank buildings, speculative securities trading, unreasonable compensation and expenses paid to directors and officers, and fraudulent "land flips" and other complex real estate transaction schemes.

As mentioned before, the FDIC and the RTC pursue those directors, officers, and other professionals who have committed fraud upon failed financial institutions if our investigation supports such allegations. However, it is not cost effective to pursue suits against such individuals when the litigation costs would exceed any collectible judgement. In those cases in which fraud or dishonest conduct by professionals is present, but in which the FDIC or the RTC determines that cost considerations prohibit filing civil suits, every effort is made to encourage and assist criminal prosecutions by the appropriate law enforcement authorities.

Fraud and dishonesty underlie FDIC claims brought under financial institutions "bankers blanket" or fidelity bonds. Fidelity bonds insure the financial institution against losses caused by the fraudulent or dishonest activity of an institution's employees. The FDIC and the RTC have aggressively pursued claims under fidelity bonds covering failed banks and thrifts. The FDIC's largest single recovery in the first

quarter of 1989, for example, involved the settlement of a bond claim for \$60 million.

Open Institution Enforcement

The Compliance and Enforcement Section of the FDIC's Legal Division provides legal support, advice, and counsel to the Division of Supervision ("DOS") and prosecutes civil enforcement actions on behalf of DOS against depository institutions or institution-affiliated parties whose activities pose a threat to depositors or the deposit insurance funds. The Compliance and Enforcement Section acts as the "district attorney's office" for DOS, which must police the banking industry through such administrative actions. DOS and Compliance and Enforcement are the first line of protection for the Federal deposit insurance funds.

The Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) greatly enhanced the enforcement powers of all of the Federal banking agencies. Civil money penalties for violations of laws, rules, regulations and orders have increased from \$1,000 per day to ranges of \$5,000 to \$1,000,000 per day per violation. Call report penalties have increased from \$100 per day per violation to ranges of \$2,000 to \$1,000,000 per day per violation. Other enforcement powers have been clarified -- such as jurisdiction over individuals separated from insured depository institutions, personal liability of individuals to insured depository institutions, records-keeping, and the like.

New enforcement powers have been added, including the right to suspend temporarily the deposit insurance of an institution operating with no tangible capital under the capital guidelines of the appropriate Federal banking agency, and the cross-guaranty provisions rendering affiliated depository institutions liable for losses reasonably anticipated by the FDIC when a commonly-controlled institution fails.

The most common administrative enforcement tool used by the FDIC is the cease-and-desist order. Cease-and-desist orders are used to halt and correct unsafe or unsound banking practices committed by state nonmember banks or individuals related to those institutions. In 1988 and 1989, the FDIC issued 98 and 97 cease-and-desist orders, respectively.

The FDIC also has the ability to terminate an insured institution's Federal deposit insurance for engaging in unsafe or unsound practices or for violations of law. As mentioned above, FIRREA also gave the FDIC the power to suspend temporarily the deposit insurance of institutions not meeting tangible capital requirements. In 1988, the FDIC initiated 77 proceedings to terminate deposit insurance. During 1989, the FDIC initiated 73 such proceedings and 1 proceeding to suspend deposit insurance temporarily.

The FDIC can remove directors, officers, and other institution-affiliated parties from any involvement in an institution's affairs if the individual violates any law or

engages in unsafe or unsound practices. The FDIC also is authorized to assess substantial civil money penalties against depository institutions and institution-affiliated parties for violations of law or outstanding enforcement orders. During 1988, the FDIC issued 33 final removal orders and assessed civil money penalties in 10 instances. In 1989, we issued 10 final removal orders and assessed civil money penalties against institutions or individuals in 9 cases. In 1990, 10 final removal orders have already been issued and 9 civil money penalties have been assessed against individuals. In general, there has been a shift in emphasis over the past few years to enforcement actions against individuals, in keeping with the FDIC's commitment to reduce insider abuse.

Cross-guaranty actions, as mentioned above, are a new enforcement power granted to the FDIC by FIRREA. In such actions, commonly-controlled depository institutions may be assessed for the loss reasonably anticipated by the FDIC due to the default of a related depository institution. The first such action was initiated in 1989.

Amendments to Senate Omnibus Crime Bill to Improve Prosecution of Thrift and Bank Fraud

On the whole, the FDIC and RTC support the thrift and bank fraud amendments passed by the Senate as part of the omnibus crime bill, S. 1970 (the "bank fraud amendments".) They would provide the FDIC and the RTC with a number of important new enforcement

tools. These new tools will allow us to combat financial institutions fraud more effectively and save money for the Federal deposit insurance funds and the taxpayers. A detailed discussion of the individual provisions of the bank fraud amendments is contained in the attachment to this statement.

Bankruptcy amendments. We strongly favor the amendments to the Federal Bankruptcy Code that would enhance the FDIC's ability to recover funds from individuals who have defrauded federally insured financial institutions. These individuals often file personal bankruptcy that results in the discharge of judgments or debts based on fraudulent, wrongful or criminal conduct. Although the FDIC has actively attempted to prevent such discharges, the Bankruptcy Code and case law interpreting it often make it difficult for the FDIC to prevent these individuals from avoiding these debts.

The bankruptcy amendments would remedy this situation. We are especially supportive of the so-called "homestead exemption" contained in those provisions. The homestead exemption would prevent individuals who have defrauded banks or thrifts from hiding their multi-million dollar homes under the protection of state law. We respectfully urge this Committee to work for the inclusion of the homestead exemption in any final fraud legislation.

Priority of claims. Section 259 is another very important provision to the FDIC and RTC. It would make the law very clear

that the FDIC and the RTC have priority over competing claims against former directors, officers, employees, accountants or other professionals that had provided services to a failed institution. This would go a long way in protecting the deposit insurance funds and the American taxpayer from the costs of bank and thrift failures.

Prejudgment attachment and fraudulent transfers. We also favor the amendment that would allow the FDIC and RTC to make prejudgment attachments of the assets of persons obligated to failed insured depository institutions. We suggest, however, that the authority be expanded to encompass enforcement actions taken by the FDIC in its corporate capacity against open institutions. We also favor the provision that would allow the FDIC to avoid certain fraudulent transfers of assets made within five years of the appointment of a receiver.

Golden parachutes. One very important area to the FDIC that is not contained in the Senate's bank fraud amendments is the authority to prohibit or limit excessive or abusive golden parachutes and similar types of payments by troubled depository institutions. The FDIC thinks it unconscionable that directors, officers and others responsible for an insured institution's failure -- or near-failure -- should be able to line their pockets with an insured institution's money at the expense of the Federal deposit insurance funds. Paying golden parachute money to a director, officer, or other responsible party in the case of a failed or failing insured institution amounts

essentially to paying that person with a check drawn on the Federal deposit insurance funds.

Golden parachute provisions are contained in the various versions of the bank fraud amendments now being considered in the House. Such provisions are very important to the FDIC and RTC in limiting the liabilities of the deposit insurance funds and taxpayers. We urge that they be included in any final legislation.

Qui tam. There are several provisions in the Senate bank fraud amendments that cause the FDIC some concern. Subtitle I of the amendments, the so-called "qui tam" provisions, would encourage private rights of action against banks and thrifts that have engaged in fraudulent activity. We have concern that these qui tam provisions could create a managerial and administrative nightmare for the FDIC and the RTC. Because private litigants have no real accountability for their actions, the FDIC and RTC would have to devote substantial resources to overseeing and monitoring those actions to ensure that they did not interfere with our own lawsuits. We could conceivably be put in the position of having to intervene as a party in some of the private suits if we thought our own positions might be adversely affected by a judicial decision. The costs to the FDIC and RTC would be significant.

The qui tam provisions run the risk of upsetting well established legal precedents, which could adversely affect the

ability of the FDIC and RTC to carry out our fundamental goals of resolving failed banks and thrifts and protecting the deposit insurance funds. We also are concerned that private parties may be less likely to share information with us on a voluntary basis if they know they can get paid for the information or use it to bring their own private rights of action. Finally, we believe that the qui tam provisions would only add to the already overloaded dockets of the Federal courts, resulting in delays of matters that the FDIC or RTC believes should have priority.

Disclosure of civil enforcement matters. We also have reservations about Section 156, which would require the disclosure of certain civil enforcement actions, because the language is somewhat unclear. The FDIC always has supported the disclosure of final enforcement orders, as evidenced by our support of the disclosure provisions contained in the Financial Institutions Reform, Recovery, and Enforcement Act of 1989. However, we cannot extend our support to publication of informal agreements since, by doing so, the force and effect of a valuable enforcement tool is taken away.

Voluntarily executed written agreements, letter agreements, business plans, and other such agreements are a valuable informal method of guiding institutions that have not deteriorated to the level of a formal enforcement action away from potential problems. Such plans are often "road maps" that provide regulatory guidance to institutions on avoiding potential trouble areas. The failure of an institution to

follow the suggestions in a plan is no guarantee that formal enforcement action will be necessary, nor is the entering of such an agreement the hallmark of a troubled institution. The willingness of institutions to enter into such agreements lies partly in the understanding that they will not be subject to public censure. By eliminating the impetus for these informal agreements, the only regulatory tool left to the agencies is the formal administrative action, which may not be appropriate for the institution.

It is our understanding that Section 156 is intended to require disclosure only of those administrative actions that are analogous to, and enforceable in the same manner as, final enforcement orders. But, it is not intended to require disclosure of informal memorandums of understanding and similar agreements that the FDIC and the other banking agencies might undertake. We believe the statutory language in Section 156 is not completely clear on this point. Thus, we would feel more comfortable if the language could be clarified to more closely mirror congressional intent that informal agreements are not required to be disclosed.

RTC Enforcement Division. We also have concerns about Section 258, which would require the creation of an RTC Enforcement Division to assist in pursuing criminal and civil claims against individuals associated with insured depository institutions. We do not believe that a separate RTC Enforcement Division is a necessary or cost-effective use of RTC resources.

The RTC already has established various units within its organizational structure to assist in pursuing claims against failed thrifts and the individuals associated with them. As outlined above, the RTC has its own "fraud squad" that investigates every single failed thrift to determine whether there is evidence of fraud or abuse that contributed to the institution's failure. The RTC also participates in bank fraud working groups and other interagency cooperative efforts to assist in the prosecution of financial institution crimes. In addition, the FDIC/RTC Legal Division brings claims against directors, officers, and other insiders to recover monies owed to the agencies. The goals of Section 258 can and are being accomplished without the necessity of micromanaging the internal structure of the RTC by requiring a separate Division.

Finally, we have reservations about Section 112. That section provides in part that a Special Counsel for the Financial Institutions Fraud Unit within the Department of Justice will be responsible for ensuring that Federal statutes relating to civil enforcement are used to the fullest extent authorized by law. While we support legislation that encourages the fullest prosecution of individuals guilty of bank fraud, we are concerned that Section 112 may unintentionally encroach on the authority of the appropriate Federal banking agencies to supervise and monitor insured depository institutions and institution-affiliated parties and to bring administrative enforcement actions against them. We would urge that this provision be clarified to ensure that the Special Counsel is

responsible for civil enforcement only with respect to statutes that are under its jurisdiction.

Conclusion

In conclusion, Mr. Chairman and members of the Committee, the FDIC and the RTC are vitally concerned with the threat that fraud and insider abuses pose to the continued safety and soundness of insured institutions and the deposit insurance funds. We believe that our aggressive enforcement efforts, the increased penalties and stronger enforcement authority provided to us in FIRREA, and the legislative initiatives now being considered by the Congress will prove to be a formidable deterrent to financial institution fraud and abuse.

FEDERAL DEPOSIT INSURANCE CORPORATION

and

RESOLUTION TRUST CORPORATION

COMMENTS ON S. 1970

AUGUST 2, 1990

This memorandum contains the FDIC's and the RTC's comments on relevant sections of S. 1970. Where appropriate, we have included in the attached Appendix revised statutory language that reflects the FDIC's and the RTC's recommended changes to the legislation. In instances where we do not specifically comment on a particular section, we either support it or defer to the Department of Justice. (Page references are to the printed amendment that was offered to S. 1970-- Document # 061012.538.)

Before beginning our comments, we want to point out that several sections of the proposed legislation use the definition of "institution-affiliated party" contained in Section 3(u) of the Federal Deposit Insurance Act. However, with regard to independent contractors such as attorneys, accountants, etc., this definition imposes a requirement that such persons act "knowingly or recklessly." In the context of bank and thrift fraud, such a standard is inappropriately strict. Therefore, we recommend that a new term, "institution-related party," be used which does not contain this "knowing or reckless" standard. [See Appendix, p. 1]

Section 112, Page 8, "Responsibilities of Special Counsel"

Paragraph (b)(2) provides that the Special Counsel for the Financial Institutions Fraud Unit within the Justice Department shall be responsible for ensuring that Federal statutes relating to civil enforcement, asset seizure and forfeiture, money laundering, and racketeering are used to the fullest extent authorized by law to attack the financial resources of persons who have committed crimes against the financial services industry.

This provision will create confusion with regard to the authority of the appropriate Federal banking agencies to supervise insured depository institutions and institution-affiliated parties and to seek compliance with federal banking laws from these institutions and individuals. We recommend that the confusion be remedied by a clarification that the Special Counsel is to use all powers available to him under Title 18 of the U.S. Code, or by legislative history that states that the authority of the Special Counsel is not intended to interfere with the civil enforcement authority of the appropriate Federal banking agencies.

Section 152, Page 14, "Restitution for Victims of Bank Crimes"

The FDIC supports this provision. Section 152 would make restitution available to all victims of an offense predicated on a scheme or conspiracy, including the FDIC and RTC, whether or not a victim is specifically named in a count of conviction. It is common in prosecutions for scheme-based offenses, such as mail fraud or bank fraud, to set forth a broad scheme victimizing numerous parties, and then set forth a limited number of events as individual acts taken in furtherance of the scheme. Some courts have permitted restitution only to the victims named in those exemplary counts. This Section imposes a common sense rule that a fraud victim's right to restitution does not depend on the prosecutor's tactical charging decisions.

Section 154, Page 16, "Nondischarge of Debts in Federal Bankruptcy Involving Obligations Arising From a Breach of Fiduciary Duty"

This section would enhance the FDIC's and RTC's ability to object to the discharge in bankruptcy of certain judgments obtained by the FDIC against institution-affiliated parties. Section 523(a)(4) of the Bankruptcy Code provides that a debt "for fraud or defalcation while acting in a fiduciary capacity" is not dischargeable. The FDIC has had difficulty using this section since bankruptcy courts look to state law to define who is a "fiduciary" and what constitutes a "defalcation." This section specifically provides that a breach of fiduciary duty by an institution-affiliated party constitutes a "defalcation" within the meaning of Section 523(a)(4).

As we noted in our general comment at the beginning of this memorandum, we recommend that the term "institution-affiliated party" be replaced with the term "institution-related party" so that independent contractors are covered without regard to whether they acted knowingly or recklessly. [See Appendix, p. 1]

Section 155, Page 16, "Disallowing Use of Bankruptcy to Evade Capital Commitments"

The FDIC strongly supports this section. However, we suggest some revisions noted below.

Section 155(a): This provision would amend Section 1141 of the Bankruptcy Code to prevent commitments to maintain the capital of federally insured financial institutions from being discharged in Chapter 11 bankruptcy proceedings. To implement the purpose of the amendment fully, however, subsections (a) and (c) of 1141 of the Bankruptcy Code need to cross reference the proposed new paragraph (d)(4) along with the present paragraphs (d)(2) and (d)(3).

This subsection will only affect corporate debtors. Individuals who are in Chapter 11 proceedings will be treated in the same manner under new Section 523(a)(11), discussed below.

Paragraph (a)(2) provides that a debtor may not be discharged in bankruptcy from his responsibilities on any commitment to maintain the capital of an insured depository institution entered into with the FDIC, RTC, OTS, etc. However, debtors may also be subject to administrative orders issued by the various Federal banking agencies to maintain the capital of insured depository institutions, pursuant to 12 U.S.C. §§ 1818(b) and (c). We recommend that the language be clarified to ensure that any responsibilities incurred under any such orders will not also be dischargeable.

Section 155(b)(1): This provision adds new subsections (a)(11), (12) and (13) to Section 523 of the Bankruptcy Code.

New Section 523(a)(11) automatically excepts from discharge debtors' obligations to honor capital maintenance commitments if the debtor is an individual in a Chapter 7 or a Chapter 11 bankruptcy proceeding. Liability for an individual in a chapter 11 proceeding is established by reading the new section together with existing section 1141(d)(2).

New Section 523(a)(12) makes criminal restitution orders that have been imposed for defrauding financial institutions nondischargeable. In Davenport v. Pennsylvania, (decided June, 1990) the Supreme Court stated that criminal restitution is dischargeable in a Chapter 13 Plan under existing Section 1328(a) of the Bankruptcy Code. New Section 523(a)(12) would close this "loophole" for debtors in any chapter in bankruptcy.

New Section 523(a)(13) of the Bankruptcy Code makes any liability imposed by a court or the appropriate financial institutions regulatory agency based upon fraud or a defalcation in a fiduciary capacity nondischargeable.

The FDIC and RTC sue many officers, directors, and controlling persons who caused losses to insured financial institutions. Although the FDIC has been successful in recovering large judgments for damages against these individuals, these individuals often use the bankruptcy system to escape paying these judgments. The FDIC has had considerable difficulty convincing the Bankruptcy Courts to find that these judgments fit into the debts currently listed in Section 523(a) as nondischargeable. The addition of 523(a)(13) will eliminate these problems.

Section 155(b)(2): This provision adds new subsections (e), (f), (g) and (h) to section 523 of the Bankruptcy Code.

New Section 523(e) clarifies that an institution-affiliated party of a depository institution is acting in a fiduciary capacity for purposes of liability under Sections 523(a)(4) and new (a)(13). This will avoid the problem we presently encounter in dealing with the term "fiduciary capacity" of having the courts construe the term so narrowly that liability usually will only be imposed upon a showing that an actual legally enforceable trust has been violated, as opposed to the general fiduciary obligations that bank directors and officers owe an institution.

New Section 523(f) removes the requirement of a financial institution regulatory agency having to show "actual reliance" on a false written statement, including a financial statement, as a condition of proving a case for an objection to the dischargeability of an obligation under Section 523(a)(2).

The FDIC often has difficulty fulfilling the "reliance" element of proof, since many times an officer or director of a failed institution did not actually rely on a false statement or false financial statement in making a loan (for example, where the borrower participated in a scheme with bank officers designed to defraud the bank.) Proposed new subsection (f) would make it clear that the FDIC and RTC need not prove that it or the failed institution relied on a false statement or false financial statement in order for a bankruptcy court to find that these types of debts, when owed to the FDIC and RTC, are not dischargeable.

New Section 523(g) extends the time for a financial regulatory agency to file complaints objecting to discharge under Sections 523 and 727 of the Bankruptcy Code. Current law requires that all complaints must be filed within 60 days after the debtor's first meeting of creditors, absent an extension being granted prior to that time. The first meeting of creditors usually occurs within 20-40 days after a bankruptcy petition is filed.

New Section 523(g) would give the FDIC 120 days from the date of the debtor's first meeting of creditors, or 120 days from the date of the appointment of a conservator or receiver of a failed financial institution (whichever is longer), to file an objection to the discharge of a particular debt of the debtor. This will avoid the situation of the institution filing on the 59th day after the first meeting of creditors and the regulatory agency missing the current 60 day deadline while it is attending to matters related to the closing of the institution. The additional time is needed in many instances because the records of failed institutions are frequently not well kept. It is often difficult to discern the existence of a bankruptcy or of information that will provide the grounds for an objection under Sections 523 or 727 of the Bankruptcy Code.

In RTC purchase and assumption transactions, many loans are transferred from a receiver to an acquiror and then can be "put" back to RTC Corporate (pursuant to the purchase and assumption agreements.) We suggest, therefore, that new section 523(g) be amended to provide that the 120 days will run from the date of the appointment of the conservator or receiver, the date of the debtor's first meeting of creditors, or the date of the "put" to RTC Corporate (whichever is longer.) Such a change will greatly assist the RTC.

New Section 523(h) adds new definitions in order to reference properly some of the terms added in the proposed amendments to Section 523 to those same terms in the Federal Deposit Insurance and Federal Credit Union Acts.

New subsection 523(h)(4) defines "institution-affiliated party" by referencing 12 U.S.C. 1813(u). As we discussed on page 1, the new term "institution-related party" should be used in order to include independent contractors without regard to whether they acted "knowingly or recklessly." [See Appendix, p. 1]

Section 155(c): This subsection amends Section 1328(a) of the Bankruptcy Code. Currently, criminal restitution and debts owed to the FDIC or RTC for money or property procured through fraud are dischargeable in a Chapter 13 plan under Section 1328(a). The amendments to Section 1328(a) provide that these debts owed to the FDIC or RTC would not be dischargeable.

This change to Chapter 13 is consistent with the changes to the other chapters of the Bankruptcy Code made by S. 1970 and keeps Chapter 13 from becoming the only remaining haven for institution-affiliated parties who caused losses to federally insured depository institutions. As a matter of technical drafting, the FDIC suggests that Section 155(c) be amended as shown in the Appendix, page 2.

Section 155(d): This subsection amends Section 522(c)(1) of the Bankruptcy Code to allow the FDIC and RTC to satisfy nondischargeable claims from exempt property of a debtor. Thus, not only will a debtor's exempt property be available to satisfy tax obligations, it will also be available to satisfy obligations due to having caused losses to federally insured financial institutions.

This subsection will keep former directors and officers from avoiding their obligations for losses they caused failed insured depository institutions by hiding their assets in property (for example, large and expensive homes) protected by the liberal exemptions provided by some States.

We have some technical suggestions to Section 155(d), which are attached at Appendix, page 3.

Section 155(e): This subsection amends Section 365 of the Bankruptcy Code to except capital maintenance responsibilities from disavowal as executory contracts. For this section to accomplish its intended purpose, however, it should be amended to limit the debtor's liability to the amount owed at the time the insured depository institution was declared insolvent. While the subsection is also intended to deal with Chapter 11 debtors who have continuing responsibilities to open institutions, a court would likely require that this claim be estimated, and it is unclear whether or not the financial status of an open insured institution could or should be estimated by a bankruptcy court.

Section 156, Page 23, "Disclosure of Civil Enforcement Actions"

The FDIC has reservations about Section 156, which would require the disclosure of certain civil enforcement actions, because the language is somewhat unclear. The FDIC always has supported the disclosure of final enforcement orders, as evidenced by our support of the disclosure provisions contained in the Financial Institutions Reform, Recovery, and Enforcement Act of 1989. However, we cannot extend our support to publication of informal agreements since, by doing so, the force and effect of a valuable enforcement tool is taken away.

Voluntarily executed written agreements, letter agreements, business plans and other such informal agreements are valuable methods of guiding institutions that have not deteriorated to the level of enforcement actions away from potential problems. Additionally, such agreements are used for institutions that are not in a troubled condition but are seeking guidance in an unfamiliar area of banking. By working closely with such institutions, potential trouble areas are avoided. The willingness of institutions to execute such agreements lies, in part, in assurances that they will not be subject to public

censure. By eliminating the impetus for these informal agreements, the only regulatory tool left to the agencies is the formal administrative action, which may not be appropriate for the institution.

It is our understanding that Section 156 is intended to require disclosure only of those administrative actions that are analogous to, and enforceable in the same manner as, final enforcement orders. But, it is not intended to require disclosure of informal memorandums of understanding and similar agreements that the FDIC and the other banking agencies might undertake. We believe the statutory language in Section 156 is not completely clear on this point. Thus, we would suggest that the language be clarified to more closely mirror congressional intent that informal agreements that are not enforceable in the same manner as final enforcement orders are not required to be disclosed.

The FDIC currently collects final orders in administrative enforcement proceedings from the regional offices and publishes them as required by FIRREA, on a monthly basis. Section 156 would require publication of an order within 30 days of agency action on the order. Consequently, the Federal banking agencies would have to continually publish new orders on a daily basis. We would prefer being able to continue our existing practice of collecting all final orders and publishing them all at once on a monthly basis.

The FDIC has no objection to a public hearing requirement; however, as a technical matter, we suggest that this amendment be made to section 8(h) of the Act, 12 U.S.C. § 1818(h), which deals with hearings.

With regard to public hearings, it would seem that making the transcripts available to the public is unnecessary and would merely create an additional expense and administrative burden to the regulatory agency.

Finally, the FDIC strongly recommends that the effective date of this provision be no earlier than the date the legislation becomes effective.

Section 251, Page 33, "Concealment of Assets from Federal Banking Agencies Established as Criminal Offense"

This Section creates the crime of knowingly concealing assets against which a federal banking agency "may have a claim." However, in the criminal context, the phrase "may have a claim" is most likely too vague to pass constitutional scrutiny. We suggest that it be replaced with language patterned on the bankruptcy fraud provisions found in 18 U.S.C. §152.

Section 252, Page 34, "Civil & Criminal Forfeiture"

The FDIC supports this provision.

Section 253, Page 36, "Civil Actions under RICO"

This section expands the civil remedies pursuant to 18 U.S.C. section 1964 and allows the Chairman of the FDIC or the Chairman of the RTC, or their designees, to institute proceedings in cases where violations affect insured depository institutions. No changes are recommended.

Section 254, Page 36, "Subpoena Authority for FDIC & RTC"

The FDIC supports this provision.

Section 255, Page 38, "Fraudulent Conveyances Avoidable by Receivers"

This provision will be a welcome tool in the continuing fight to combat financial institution fraud. Section 255 provides the FDIC and RTC with the ability to avoid fraudulent transfers of assets by institution-affiliated parties and debtors, if the transfers were made within 5 years of the appointment of the receiver. (It is important to note that the definition of "institution-affiliated party" should be changed, or the new term "institution-related party" suggested above be used, in order to include independent contractors without regard to whether they act knowingly and recklessly.)

While the avoidance of fraudulent conveyances is a necessary and desirable power, the precise language of Section 255 might not be broad enough to prevent an analogous abuse. We have seen institutions, in contemplation of insolvency, formally release the personal guarantor of a loan. While such a release arguably does not involve a conveyance, the result is a reduction in the value of receivership assets just as if receivership property had been transferred. We would suggest broadening the language to prohibit such fraudulent extinguishment of obligations as well.

The FDIC also suggests that this Section be revised to provide that attempts to defraud the FDIC or other federal banking agencies also will result in an avoidable transfer. The provision as written is limited to fraud against the depository institution.

Further, we would add a provision that would set aside constructive fraudulent transfers (this section is currently directed at actual fraud.) We suggest a provision similar to that found in Section 548(a)(2) of the Bankruptcy Code.

Finally, this section should be amended to provide that the rights of the FDIC and RTC take precedence over the rights of a trustee in bankruptcy. Without this provision, if an institution-affiliated party filed bankruptcy it would be able (as debtor in possession, which has all the powers of a bankruptcy trustee) to argue that 12 U.S.C. 1821(d)(17) is superseded by the Bankruptcy Code with the result that 1821(d)(17) would be rendered meaningless. [See Appendix, p. 4]

Section 256, Page 39, "Prejudgment Attachments"

The FDIC supports this provision. Proposed new paragraph 18 amends Section 11(d) of the FDI Act (12 U.S.C. § 1821(d)) to provide generally for prejudgment attachment of the assets of any person obligated to failed insured depository institutions. The FDIC's recommended changes to the provision clarify the ability of the FDIC and RTC to request a prejudgment attachment in connection with any of the powers conferred on them as a receiver or liquidator by Sections 11, 12 and 13 of the Act, and deletes what appears to be an unnecessary "willfulness" requirement if the term "institution-affiliated party" is used instead of "institution-related party." (As discussed earlier on page 1 hereof.)

With regard to paragraph 4(A) on page 41, if pre-judgment attachment is limited only to section 8(i) offenses, the FDIC will lose a valuable tool in conserving assets in a restitution/reimbursement action. Thus, we also recommend that this section be changed to encompass actions under all of Section 8, as well as Sections 7 and 18 of the FDI Act.

Additionally, in the portion of this proposed legislation which proposes to amend section 8(i) of the Act, the term "court" is not defined. Since 8(i) deals with administrative hearings, it seems that perhaps the best way to accomplish this process is to require that application be made in federal court while the administrative action is pending. Section 8(h) of the FDI Act deals with hearings and judicial review. We therefore propose that this provision be added to section 8(h) of the Act, and expanded to include all civil money penalties issued by the appropriate Federal banking agency, as well as restitution/reimbursement actions.

Finally, the FDIC recommends that the power to utilize such attachments be expanded to include situations where the FDIC can demonstrate that fraud has occurred. This would parallel at

least one favorable court decision obtained in the Fifth Circuit.
[See Appendix, p. 5]

Section 257, Page 42, "Injunctive Relief"

Section 257 would provide authority for the FDIC, NCUA or RTC, acting in any capacity, in actions involving a scheme to defraud a financial institution, to seek injunctive relief from threatened loss without a showing of special or irreparable injury. It also provides for preliminary relief when assets may be dissipated or placed beyond the jurisdiction of the court.

We view this authority as a complement to the pre-judgment attachment authority contained in the preceding section 256. Taken together, the concepts of enjoining dissipation or expatriation of assets and prejudgment attachment are powerful weapons for the bank regulatory community. Because of the closely related nature of the two forms of relief, we believe the standards and availability of the relief should be conformed in all major respects.

In the present draft, availability of pre-judgment attachment is restricted to the FDIC in its conservatorship or receivership capacities. By contrast, injunctive relief is available to the FDIC, NCUA and RTC in all capacities. We see no reason for this distinction, and believe that all forms of prejudgment relief should be available without regard to the capacity in which an action is brought, and to all federal banking agencies.

In addition, we note that the standard for preliminary injunctive relief, which is modeled after the standard in section 256, is crafted in contemplation of an action brought in a conservatorship or receivership capacity, as demonstrated by repetitive references to "the institution." By contrast, the standard for entry of permanent relief is broader and less precise.

We would suggest that the provisions of sections 256 and 257 be combined to achieve uniform availability and to apply common standards in support of appropriate relief. We would be happy to provide alternate language.

Section 258, Page 46, "RTC Enforcement Division"

It is the RTC's position that this section is unnecessary. The RTC already has units which accomplish this function. Also, for Congress to mandate a particular structure to an agency greatly reduces that agency's flexibility to respond to new and unforeseen events.

Section 259, Page 47, "Priority of Certain Claims"

The FDIC supports Section 259, subject to the suggested changes described below. Section 259 recognizes that multiple claims for personal damages are frequently brought by shareholders, depositors and creditors following a financial institution failure. These claims compete with FDIC or RTC claims or actions against the same parties for damages suffered by the financial institution and the deposit insurance funds. The high cost of defending against multiple claims not only outstrips the personal financial resources of most defendants, but also quickly depletes even the largest professional liability insurance policies which often contain standard "wasting" provisions that allow the payment of defense costs out of the coverage limits.

Section 259 has been drafted to grant the FDIC and RTC a clear priority over such competing claims. The effect of this provision will be to allow the FDIC and RTC time to investigate and prosecute claims against former directors and officers and other professionals for losses caused the failed institution by their gross negligence, breaches of fiduciary duty, fraud or other wrongdoing. Thus, suits by the FDIC and RTC will be allowed to recoup losses on behalf of the insurance funds and other creditors of the failed institutions first before any competing claimants. This provision will greatly enhance the ability of the FDIC and RTC to recover against these parties for the benefit of the insurance funds by staying the prosecution of competing claims until the FDIC and RTC's claims are satisfied through settlement or post-judgment execution.

Although the FDIC and RTC support the priority provision, there are a number of concerns regarding the effect of the broad exception for "claims of other Federal agencies of the United States" in paragraph (a) on page 48. This broad exception will vitiate the priority proposal by allowing, for example, claims brought by the Attorney General for civil money penalties for financial crimes under Section 951 of FIRREA to proceed before FDIC or RTC claims are satisfied. We would suggest that this exception be narrowed to claims of federal agencies under Section 6321 of the Internal Revenue Code of 1986 (regarding liens for unpaid taxes) and under Section 3713 of Title 31, United States Code (regarding other government claims for indebtedness). Also, the priority should apply to any claim under section 12 of the FDI Act, as well as sections 11 and 13 which are already included. In addition, we suggest that a sentence be added to subsection (a) of this section to make it clear that the priority extends to the prosecution of any suit and the execution and satisfaction of any subsequent judgement. We have attached suggested language. [See Appendix, p. 6]

We also recommend that paragraph (a)(1) be revised to clarify the priority and need for notice over competing claims that are pending at the time the Corporation acquires its claims.

The final sentence of paragraph (a)(2), on page 49, is unclear. It should be redrafted to make it clear that the FDIC will not have a priority if a court finally adjudicates that the assets in question are unavailable to satisfy judgments obtained by the FDIC or RTC.

Finally, we suggest the following explanatory language concerning the prospective applicability of this provision:

Section 259 would provide a priority for the FDIC over certain competing claims against directors, officers, accountants, attorneys and other parties. Several trial courts previously recognized this priority while others did not. Most recently a federal appeals court reversed a district court order which had recognized the priority. Section 259 would clearly grant the FDIC a priority as to claims which are filed after enactment. With regard to pending claims, the provision will be completely neutral. That is, it should neither support nor undercut any party's position with regard to whether the FDIC is already entitled to a priority under existing law.

Section 260, Page 49, "Expedited Procedures for Certain Claims"

The FDIC supports this provision; however, we recommend that the 10, 60 and 90 day time frames be lengthened to 30, 120 and 180 days, respectively.

Section 351, Page 51, "Interagency Coordination"

This section specifically authorizes the agencies to provide and the Attorney General to accept the assistance of agency attorneys and investigative personnel to assist the Department of Justice in the prosecution of crimes affecting savings associations.

In principle, we support this provision, although we see no real need for it. The Department of Justice already can reach the same result through designation of agency attorneys as Special Attorneys or Special Assistant U.S. Attorneys and designation of other agency employees as agents of a grand jury.

Section 352, Page 52, "Foreign Investigations"

The FDIC is of the opinion that this provision is unnecessary since these functions are already being accomplished.

Sections 401-469, Page 55, "Private Rights of Action"

While the FDIC acknowledges that these sections of the bill have been amended in an effort to address some of the concerns that we have previously expressed, it is still our opinion that these legislative initiatives would substantially burden the supervisory function and, therefore, we cannot endorse them.

New Section 503, Page 90, "Clarification of FDIC Authority"

This is a new section that will cure a major problem that the FDIC is currently facing with respect to FSLIC Resolution Fund institutions.

The FSLIC Resolution Fund provisions, as currently codified, create two basic problems:

1. The Corporation, in managing the FRF, is not explicitly given any of its normal powers under Sections 9, 11, 12, 13 or 15 of the FDI Act.
2. Nowhere in FIRREA is the FDIC explicitly appointed receiver for savings and loan associations that failed prior to January 1, 1989.

These two problems have been exhibited in many different ways. When the FDIC, as receiver for pre-January 1, 1989 receiverships, has brought suit to collect on notes, litigants have argued that the FDIC is not the receiver for these institutions. They have alternatively argued that even if the FDIC is receiver, it has none of its receivership powers under Section 11 of the FDI Act. Similarly, certain title insurance companies have refused to issue title insurance to FDIC as receiver, arguing that they cannot find any reference to these pre-January 1, 1989 receiverships in FIRREA. Similar problems exist when the FDIC has attempted to collect on assets that are in the FRF.

In crafting a legislative clarification of FIRREA to correct these problems, it is important to maintain the distinction between FRF assets and liabilities and the assets and liabilities of each of the pre-January 1, 1989 receiverships. The FSLIC Resolution Fund is only composed of those assets and liabilities

that belonged to FSLIC in its corporate capacity (i.e., those assets that the FSLIC corporate purchased as part of its S&L assistance agreements). The pre-January 1, 1989 receivership estates each have their own assets and liabilities. Any receivership liability can only be paid from the liquidation of that failed institution's assets. If this distinction were to be blurred, the FRF could become responsible for these receivership liabilities.

To clarify FIRREA and correct the existing problems we need the two provisions set forth below. However, the more important of the two provisions is paragraph (9).

Section 11(a) of the Federal Deposit Insurance Act (12 U.S.C. § 1821(a)) is amended by inserting after subsection (7) the following new paragraphs:

"(8) Use of FDIC Powers. -- As of August 10, 1989, the Corporation shall have the same rights, powers and authorities to carry out its duties with respect to the assets and liabilities of the FSLIC Resolution Fund as the Corporation has under sections 9, 11, 12, 13 and 15 with respect to insured depository institutions."

"(9) Corporation as Receiver. -- As of August 10, 1989, the Corporation shall succeed the Federal Savings and Loan Insurance Corporation as conservator or receiver with respect to any institution for which the Federal Savings and Loan Insurance Corporation was appointed conservator or receiver on or before December 31, 1988. When acting as such conservator or receiver, the Corporation shall have all of the rights, powers and authorities as the Corporation has as a conservator or receiver under this Act."

FDIC & RTC COMMENTS ON S. 1970

APPENDIX

Section [], Page [], "Definitions"

On page [], line [], insert the following new subsection:

"A new section 3(y) shall be added to The Federal Deposit Insurance Act, 12 U.S.C. 1813(y), as follows:

(y) INSTITUTION-RELATED PARTY.-- The term "institution-related party" shall mean any insured depository institution's director, officer, employee, agent, attorney, accountant, appraiser or any other party employed by or providing services to an insured depository institution."

Section 155, Page 21, "Disallowing Use of Bankruptcy to Evade Capital Commitments"

On page 21, line 16, substitute the following section:

"(c) PLANS UNDER CHAPTER 13.-- Section 1328(a)(2) of Title 11, United States Code, is amended to read as follows:

"(2) of a kind specified in--

"(A) section 523(a)(5), (7), (11), (12) or (13) of this title; or

"(B) section 523(a)(2), (4) or (6) of this title, when such debts are owed to the appropriate Federal financial institutions regulatory agency (as defined in section 8(e)(7)(D) of the Federal Deposit Insurance Act (12 U.S.C. 1813(e)(7)(D)), and in addition includes the Resolution Trust Corporation, and includes such an agency or corporation whether it is acting in its capacity as a conservator or receiver or in its corporate capacity, or a conservator or receiver of an insured depository institution (as defined in section 3(c)(2) of the Federal Deposit Insurance Act (12 U.S.C. 1813(c)(2))) or insured credit union (as defined in section 101(7) of the Federal Credit Union Act (12 U.S.C. 1752(7)))."

Section 155(d), Page 22, "Disallowing Use of Bankruptcy to Evade Capital Commitments"

On page 22, line 10, substitute the following section:

"(d) EXEMPTION OF PROPERTY.-- Section 522(c)(1) of Title 11, United States Code, is amended to read as follows:

"(1) a debt of a kind specified in--

"(A) section 523(a)(1), (5), (11), (12) or (13) of this title; or

"(B) section 523(a)(2), (4) or (6) of this title, when such debts are owed to the appropriate Federal financial institutions regulatory agency (as defined in section 8(e)(7)(D) of the Federal Deposit Insurance Act (12 U.S.C. 1813(e)(7)(D)), and in addition includes the Resolution Trust Corporation, and includes such an agency or corporation whether it is acting in its capacity as a conservator or receiver or in its corporate capacity, or a conservator or receiver of an insured depository institution (as defined in section 3(c)(2) of the Federal Deposit Insurance Act (12 U.S.C. 1813(c)(2))) or insured credit union (as defined in section 101(7) of the Federal Credit Union Act (12 U.S.C. 1752(7)))."

Pages 38-39, Section 255, "Fraudulent Conveyances"

On page 38, line 13, delete the word "affiliated" and insert in its place the word "related"

On page 38, line 21, after the word "involuntarily" insert a dash, delete the remainder of that sentence and add the following:

"(1) made such transfer or incurred such liability with actual intent to hinder, delay, or defraud the insured depository institution, the Corporation or any appropriate Federal banking agency; or

(2)(A) received less than a reasonably equivalent value in exchange for such transfer or obligation; and

(B)(i) was insolvent on the date that such transfer was made or such obligation was incurred, or became insolvent as a result of such transfer or obligation;

(ii) was engaged in business or a transaction or was about to engage in business or a transaction, for which any property remaining with the institution-related party or debtor was unreasonably small capital; or

(iii) intended to incur, or believed that the institution-related party or debtor would incur, debts that would be beyond the institution-related party's or debtor's ability to pay as such debts matured."

On page 39, line 23, insert the following new subparagraph:

"(D) RIGHTS UNDER THIS SECTION.-- The rights of the Corporation under this section shall be superior to any rights of a trustee or any other party under Title 11."

Pages 39-42, Section 256, "Prejudgment Attachments"

On page 40, lines 6-8, delete the words "(in the Corporation's capacity as conservator or receiver for any insured depository institution)," and insert the words "in connection with exercising the powers conferred by this section and Sections 12 and 13 of the Act,"

On page 40, line 13, delete the word "affiliated" and insert the word "related"

On page 40, line 14, insert the words "or may be" after the word "is"

On page 40, line 22, insert the words "or that the Federal banking agency can demonstrate that a fraud has occurred" after the word "appointed"

On page 40, line 23, delete the words "Section 8(i)" and insert instead "Section 8(h)"

On page 40, line 24, delete the words "(12 U.S.C. 1818(i))" and insert instead "(12 U.S.C. 1818(h))"

On page 41, line 3, delete the words "including actions brought in aid of, or to enforce an order in, any other civil or administrative action for money damages, restitution, or injunctive relief brought by such agency or corporation" and insert instead "this section, or section 7 or 18 of this Act"

On page 41, line 6, insert after "corporation" the following:

"to the United States district court, or the United States court of any territory, within the jurisdiction of which the home office of the depository institution is located, the court may"

Page 47, Section 259, "Priority of Certain Claims"

On page 47, line 23, insert a comma and the number "12" after the number 11.

On page 48, lines 6-7, delete the words "or the United States" and insert the words "under Section 6321 of the Internal Revenue Code of 1986 and Section 3713 of Title 31, United States Code,"

On page 48, line 11, after the word "notice" insert the words "of the commencement of such other suit, claim or cause of action or, in the event that a suit, claim or cause of action is pending at the time the Corporation acquires claims under Section 11, 12 or 13 of the Act, 180 days after receiving written notice of such pending suit, claim or cause of action,"

On page 48, line 13, after the word "to" delete the words "file suit" and insert the words "pursue potential claims against such party", and after the word "diligently" delete the word "pursuing" and insert the word "investigating"

On page 49, lines 1-3, delete the entire sentence and insert in its place the following: "This provision shall not afford the Corporation priority as to any asset which is finally adjudicated to be unavailable to satisfy any subsequent judgment obtained by the Corporation as a result of its suit, claim or cause of action."

On page 49, line 3, add the following sentence: "This priority shall apply to both the prosecution of any suit claim or cause of action, and to the execution and satisfaction of any subsequent judgment resulting from any suit claim or cause of action."